

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 93-583-W - ORDER NO. 94-656 ✓
JULY 13, 1994

IN RE: Application of Hyde Park Water Works,) ORDER APPROVING
 Inc. for an Increase in Water Rates) RATES AND
 and Charges.) CHARGES

This matter comes before the Public Service Commission of South Carolina (the Commission) by way of an Application filed by Hyde Park Water Works, Inc. (Hyde Park or the Company) on February 28, 1994, for an increase in its rates and charges for water service provided to its customers in Greenwood County, South Carolina. The application was filed pursuant to S.C. Code Ann. §58-5-240 (1976), as amended, and 26 S.C. Regs 103-821 (1976).

By letter dated March 29, 1994, the Commission's Executive Director instructed the Company to publish a prepared Notice of Filing, one time, in a newspaper of general circulation in the area affected by the Company's Application. The Notice of Filing indicated the nature of the Company's Application and advised all interested parties of the manner and time in which to file appropriate pleadings for participation in this Docket. Additionally, the Company was instructed to directly notify all of its customers affected by the proposed increase. The Company submitted affidavits indicating it complied with these instructions. A Petition to Intervene was filed by the Consumer Advocate for the State of South Carolina (Consumer Advocate). By

letter dated June 27, 1994, the Consumer Advocate informed the Commission that its concerns in this matter were satisfied and that the Consumer Advocate would not participate in the hearing in this matter.

The Commission Staff made on-site investigations of the Company's facilities, audited the Company's books and records, and gathered other detailed information concerning the Company's operations.

On June 29, 1994, a public hearing concerning the matters asserted in the Company's Application was held in the Commission's Hearing Room. Pursuant to S.C. Code Ann. §58-3-95 (Supp. 1993), a panel of three (3) Commissioners, Commissioners Mitchell, Butler, and Bowers, was designated to hear and rule on this matter. Commissioner Mitchell presided. Hyde Park was not represented by counsel, and the Commission Staff was represented by Florence P. Belser, Staff Counsel.

The Company presented the testimony of Don Smith, President of Hyde Park. The Commission Staff presented the testimony of Steve W. Gunter, Utilities Accountant, and William O. Richardson, Utilities Engineer Associate III.

FINDINGS OF FACT

Based upon the Company's Application, the testimony and evidence received into evidence at the hearing, and the entire record of these proceedings, the Commission now makes the following findings of fact:

1. Hyde Park is a water utility providing water service in its service area within South Carolina, and its operations are

subject to the jurisdiction of the Commission, pursuant to S.C. Code Ann. §58-5-10, et seq. (1976), as amended. Hyde Park provides service to 91 customers in Greenwood County.

2. The Company's present rates and charges were approved by Order No. 91-638, dated July 29, 1991, in Docket No. 90-713-W.

3. The appropriate test period for the purposes of this proceeding is the twelve-month period ending December 31, 1993.

4. By its Application, the Company is seeking an increase in its rates and charges for water service of \$4,894 which Staff has calculated to be \$5,910. Hyde Park currently charges its customers a flat monthly fee of \$10.00 per month; it is seeking approval to charge a flat monthly fee of \$15.00 per month.

5. The appropriate operating revenues for the Company for the test year under present rates and after accounting and pro forma adjustments are \$10,470 which reflects a decrease in per book revenues of (\$1,136).

6. The appropriate operating revenues under the proposed rates are \$16,380.

7. The appropriate operating expenses for the Company's operations for the test year under its present rates and after accounting and pro forma adjustments are \$9,430 which reflects an increase in per book expenses of \$135.

8. The appropriate operating expenses under the approved rates are \$10,614.

9. The Company's reasonable and appropriate federal and state income tax expense should be based on the use of a 15.0% federal tax rate and a 5.0% state tax rate, respectively.

10. The Company's appropriate level of net operating income for return during the test year under its present rates after accounting and pro forma adjustments is \$1,040.

11. The Company should have the opportunity to earn a 35.20% operating margin which is produced by the appropriate level of revenues and expenses found reasonable and approved herein. The Commission finds that this operating margin is fair and reasonable.

12. The rate schedule approved by the Commission herein is appropriate and should be adopted.

13. The rates and charges depicted in Appendix A, attached hereto and incorporated by reference, are approved and effective for service on or after the date of this Order.

EVIDENCE AND CONCLUSIONS

EVIDENCE AND CONCLUSIONS FOR FINDING OF FACT NOS. 1 AND 2.

The evidence supporting these findings concerning the Company's business and legal status is contained in the Company's Application and in prior Commission Orders in the docket files of which the Commission takes notice. These findings of fact are essentially informational, procedural, and jurisdictional in nature, and the matters which are involved are essentially uncontested.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NOS. 3 AND 4.

The evidence for these findings concerning the test period and the amount of the revenue increase requested by the Company is contained in the Application of Hyde Park and the testimony of Company witness Don Smith, President of Hyde Park, and Staff witnesses Steve W. Gunter and William O. Richardson.

On February 28, 1994, the Company filed an Application requesting approval of a rate schedule designed to produce an increase in gross revenues of \$4,894 which Staff calculated, using the appropriate billing units, to be \$5,910. The Company's filing was based on a test period consisting of the 12 months ending December 31, 1993. The Commission Staff likewise offered their evidence within the context of that same test period.

A fundamental principle of the ratemaking process is the establishing of a test year period. The reliance upon the test year concept, however, is not designed to preclude the recognition and use of other historical data which may precede or postdate the selected twelve month period.

Integral to the use of a test year, representing normal operating conditions to be anticipated in the future, is the necessity to make normalizing adjustments to the historic test year figures. Only those adjustments which have reasonable and definite characteristics, and which tend to influence reflected operating experiences are made to give proper consideration to revenues, expenses, and investments. Parker v. South Carolina Public Service Commission, et al., 280 S.C. 310, 313 S.E.2d 290 (1984). Adjustments may be allowed for items occurring in the historic test year, but which will not recur in the future; or to give effect to items of an extraordinary nature by either normalizing or annualizing such items to reflect more accurately their annual impact; or to give effect to any other item which should have been included or excluded during the historic test year. The Commission finds the twelve months ending December 31, 1993, to be the

reasonable period for which to make its ratemaking determinations herein.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT

NOS. 5, 6, 7, 8, AND 9.

The evidence for the findings concerning the adjusted level of operating revenues and expenses is found in the testimony and exhibits of Company witness Smith and Commission Staff witnesses Gunter and Richardson. The Staff adjusted the Company's revenues to correct an error in the Company's books and records, to remove the DHEC surcharge fee being collected by the Company as a separate line item, and to annualize revenues based on year end customers at the presently approved rate. Therefore, for the purposes of this proceeding, the appropriate operating revenues for the Company for the test year under the present rates and after accounting and pro forma adjustments are \$10,470 which reflects a decrease of (\$1,136) in revenues. Using Finding of Fact No. 10 and the Evidence and Conclusions, infra., approving a 35.20% operating margin, the Company's operating revenues after the proposed increase are \$16,380.

The Staff adjusted the Company's expenses to annualize wages based on year end employees and to remove payments to DHEC under the Federal Safe Drinking Water Act. The Staff also made adjustments to reflect the effect of the payroll tax after annualizing wages and to true-up taxes based on as adjusted income before tax. Therefore, the appropriate operating expenses for the test year under the present rates and after accounting and pro forma adjustments are \$9,430 which reflects an increase in per book

expenses of \$135. Using Finding of Fact No. 10 and the Evidence and Conclusions, infra., approving a 35.20% operating margin, the appropriate operating expenses under the approved rates are \$10,614.

The Commission concludes that each of the adjustments proposed by the Commission Staff is appropriate and is hereby adopted by the Commission. The Commission notes that the Company did not contest the Staff's adjustments.

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NO. 10.

Based on the Commission's determinations concerning the accounting and pro forma adjustments to the Company's revenues and expenses, and its determination as to the appropriate level of revenues and expenses, net income for return is found by the Commission as illustrated in the following Table:

<u>TABLE A</u> <u>NET INCOME FOR RETURN</u>	
BEFORE RATE INCREASE	
Operating Revenues	\$ 10,470
Operating Expenses	<u>9,430</u>
Net Operating Income	1,040
Customer Growth	<u>-0-</u>
Net Income for Return	<u>\$ 1,040</u>

EVIDENCE AND CONCLUSIONS FOR FINDINGS OF FACT NO. 11, 12, AND 13.

Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944), this Commission does not ensure through regulation that a utility will produce net revenues.

As the United States Supreme Court noted in the Hope Natural Gas decision, supra, the utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility and ... that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

Neither S.C. Code Ann. §58-5-290 (1976) nor any other statute prescribes a particular method to be utilized by the Commission to determine the lawfulness of the rates of a public utility. For ratemaking purposes, this Commission examines the relationships between expenses, revenues, and investment in an historic test period because such examination provides a constant and reliable factor upon which calculation can be made to formulate the basis for determining just and reasonable rates. This method was recognized and approved by the Supreme Court for ratemaking purposes involving utilities in Southern Bell Telephone and Telegraph Co. v. The Public Service Commission of S.C., 270 S.C. 590, 244 S.E. 2d 278 (1978).

For water utilities, where the utility's rate base has been substantially reduced by customer donations, tap fees, contributions in aid of construction, and book value in excess of investment, the Commission may decide to use the "operating ratio"

and/or "operating margin" as guides in determining just and reasonable rates, instead of examining the utility's return on its rate base. The operating ratio is the percentage obtained by dividing total operating expenses by operating revenues. The obverse side of this calculation, the operating margin, is determined by dividing net operating income for return by the total operating revenues of the utility.

In this proceeding the Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and, if necessary, the fixing of just and reasonable rates. This method was recognized as an acceptable guide for ratemaking purposes in Patton v. South Carolina Public Service Commission, 280 S.C. 288, 312 S.E. 2d 257 (1984).

The following Table indicates the Company's gross revenues for the test year, after accounting and pro forma adjustments under the presently approved rate schedule; the Company's operating expenses for the test year after accounting and pro forma adjustments; and the operating margin under the presently approved rate schedule for the test year:

TABLE B
OPERATING MARGIN

BEFORE RATE INCREASE	
Operating Revenues	\$ 10,470
Operating Expenses	9,430
Net Operating Income	<u>1,040</u>
Add: Customer Growth	<u>-0-</u>
Total Income for Return	<u><u>1,040</u></u>
Operating Margin (After Interest)	<u><u>9.93%</u></u>

The following Table shows the effect of the Company's proposed rate schedule, after accounting and pro forma adjustments approved herein:

TABLE C	
NET INCOME FOR RETURN	
AFTER RATE INCREASE	
Operating Revenues	\$ 16,380
Operating Expenses	10,614
Net Operating Income	<u>5,766</u>
Add: Customer Growth	-0-
Total Income for Return	<u><u>5,766</u></u>

The Commission is mindful of those standards delineated in the Bluefield decision, supra, and of the balance between the respective interests of the Company and of the consumer. The Commission has considered the spectrum of relevant factors in this proceeding: the revenue requirements of the Company, the proposed price for which the Company's service is rendered, the quality of that service, and the effect of the proposal upon the consumer, among others.

The three fundamental criteria of a sound rate structure have been characterized as follows:

...(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships between costs incurred and benefits received.

Bonbright, Principles of Public Utility Rates (1961), p. 292.

The Commission has considered the proposed increase presented by the Company in light of the various standards to be observed and the interests represented before the Commission. The Company presented the testimony of witness Smith who explained that Hyde Park was incurring increased expenses and that some expenses were paid with his personal funds. Witness Smith also testified of needed repairs and improvements to the system and of the estimated costs associated with these repairs and improvements.

The Commission must balance the interests of the Company -- i.e. the opportunity to make a profit or earn a return on its investment, while providing adequate water service -- with the competing interests of the ratepayers -- to receive adequate service at a fair and reasonable rate. In weighing these considerations, the Commission notes that Mr. Smith has been personally paying some of the Company's expenses and that he intends to make necessary repairs and improvements to the system. Consequently, the Commission finds that Hyde Park should have an opportunity to earn a 35.20% operating margin. This operating margin requires annual operating revenues of \$16,380. The following Table reflects an operating margin of 35.20%:

TABLE D
OPERATING MARGIN

AFTER RATE INCREASE	
Operating Revenues	\$ 16,380
Operating Expenses	<u>10,614</u>
Net Operating Income	<u>5,766</u>
Add: Customer Growth	<u>-0-</u>
Total Income for Return	<u><u>5,766</u></u>
Operating Margin (After Interest)	<u><u>35.20%</u></u>

In order to produce the revenues necessary to provide the opportunity to earn an operating margin of 35.20%, Hyde Park would need to charge its customers \$15.00 per month. The Commission concludes that \$15.00 per month is a fair and reasonable rate for water service provided by Hyde Park. Further, the Commission finds and concludes that the rates and charges approved herein achieve a balance between the interests of the Company and those of the customers. These rates and charges result in a reasonable attainment of the Commission's ratemaking objectives in light of applicable statutory safeguards.

IT IS THEREFORE ORDERED THAT:

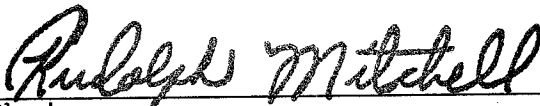
1. The schedule of rates and charges attached hereto as Appendix A is hereby approved for service rendered on or after the date of this Order. The schedule is deemed filed with the Commission pursuant to S.C. Code Ann. §58-5-240 (1976), as amended.

2. Should these schedules not be placed into effect until three (3) months from the effective date of this Order, the schedule shall not be charged without written permission from the Commission.

3. The Company shall maintain its books and records in accordance with the NARUC System of Accounts for Class C Water Utilities, as adopted by this Commission.

4. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:


Chairman

ATTEST:


Deputy Executive Director

(SEAL)

APPENDIX A

HYDE PARK WATER WORKS, INC.
110 HALTIWANGER ROAD
GREENWOOD, S. C. 29649
(803) 229-6453

FILED PURSUANT TO:

DOCKET NO. 93-583-W

ORDER NO. 94-656

EFFECTIVE DATE: JULY 13, 1994

WATER SERVICE

MONTHLY SERVICE CHARGE - FLAT RATE-----\$15.00